COMAPANY LAW STUDY MATERIAL (LAW 507)

UNIT II

(MAJOR DOCUMENTS OF A COMPANY)

BY

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1. MEMORANDUM OF ASSOCIATION

The Memorandum of Association is a sacred document for a company that defines the scope of its operations and the relationship that it shares with the shareholders. It lays down the basic features of a company. It states the name of the company, its registered office and its objectives. Section 2(56) of the Companies Act, 2013, states that Memorandum is the "*memorandum of association of a company as originally framed or as altered from time to time in pursuance of any previous company law or of this Act*".

- **Name clause**

The name clause contains the name of the company. Since a company is an artificial juristic person and has an identity distinct from that of its members, it must have a name by which it can enter into contracts and purchase property. The name of the company must not be similar to that of an existing company. Moreover, the company must not adopt a name whose use is prohibited by the law of the land. In the case of a public company, the name of the company ends with 'Ltd.' and if the company is a private company, then the name of the company ends with 'Pvt. Ltd.'.

- **Registered office clause**

The company must specify the name of the state in which it is going to establish its registered office. If, after incorporation, the company decides to shift its registered office to any other state, then the company will have to alter its MoA through a special resolution. In the case of the transfer of a registered office, the company is also under an obligation to ensure that its creditors are not adversely affected by the transfer.

- **Object clause**

The objects clause embodies the purpose and objectives for which the company is formed. Under Indian law, the subscribers to the MoA, known as the promoters, have the absolute freedom to determine the objectives of the company. The 2013 Act stipulates no requirement for separately mentioning the main and ancillary objects. However, the promoters may nonetheless choose to specify the ancillary objects along with the main objects.

The primary purpose of the object clause is to impose certain restrictions on the scope of the company's activities. It defines the scope of a company's operations, and thus, shareholders are able to make an informed choice while investing their funds. The objects clause informs the shareholders of the nature of activities in which the company might deploy its funds.

It is pertinent to note that Indian jurisprudence surrounding company law has been very much influenced by British law. As per the Companies Act, 2006 (applicable in the

United Kingdom), a company is required to file the MoA and the registration application with the Registrar at the time of the company's formation. However, the UK law does not make it mandatory to specify the objects of the company in the MoA. It does require the company to specify its name, registered office and the liability of its members.

The MoA may also state any matter that is necessary to be undertaken by the company for the purpose of attaining its objectives. However, even if a company does not mention such matters in its MoA, these operations are usually permitted by way of reasonable construction. The courts of law allow a company to undertake all such actions that are necessary for the purpose of realising its objects.

- **Liability clause**

This clause states the liability that would be borne by the members of the company. For instance, if the members are to bear limited liability, then the MoA must state that the members' liability would be limited by shares. Similarly, if the liability is to be limited by guarantee, then the MoA must specify the assets that would be contributed by each member in the event of winding up.

- **Capital clause**

The capital clause specifies the nominal capital of the company. It states the paid-up share capital of the company and the number of shares into which the capital is divided. A public company may have equity share capital, preference share capital or both.

A company cannot issue shares in excess of the number stated in the MoA. If the company wants to issue more shares, then it will have to amend its MoA in accordance with the provisions laid down in Section 61. Section 61 empowers the company to alter its share capital and even consolidate its shares by passing a resolution in the general meeting. However, any consolidation of shares that affects the voting rights of the existing shareholders will have to be approved by the National Company Law Tribunal.

Earlier, it was mandatory for a private company to have a minimum paid-up share capital of Rs. 1,00,000. Similarly, the minimum mandatory paid-up share capital for a public company was Rs. 5,00,000. However, the requirement of a minimum paid-up capital was deleted by the 2015 Amendment.

- **Subscription clause**

The last clause of the MoA is the subscription clause, which is signed by the first shareholders of the company. The subscribers declare their intention of forming a company and agree to subscribe to a specific number of shares of the company. These subscribers are also called the promoters of the company. In the case of a private company, the MoA must be subscribed to by at least 2 persons, and in the case of a public company, the MoA must be subscribed to by at least 7 persons.

1.1. Alteration of Memorandum of Association (MoA) under Section 13 of Companies Act 2013

Section 13 deals with the process of altering a 'memorandum' of a company. *Section 2(56)* provides that a memorandum means the memorandum of association of a company. *Section 2(3)* of the Act defines the terms 'alter' or 'alteration' as the act of making any omission, substitution or addition.

As per *Section 13,* a company needs to pass a special resolution in order to alter its memorandum of association. In the event of a change in the name of the company or a change in the registered office of the company, the approval of the Central Government would also be required. A company has to file the special resolution and the Central Government approval with the Registrar of Companies.

Till the 1980s, the MoA was considered an unalterable document, and thus the law imposed several restrictions on the alteration of the MoA. The company had to seek approval of external statutory bodies for the purpose of amending its MoA. The MoA defines the most important characteristics of the company, and thus, it is desirable that the clauses of the MoA not be frequently altered.

Even though the provisions relating to MoA alteration have been relaxed under the 2013 Companies Act, Section 13 lays down specific rules for the alteration of the MoA. The provisions of Section 13 apply to the alteration of the name clause, registered office clause, object clause and liability clause of the MoA. The capital clause can be amended by an ordinary resolution.

- ***Change in name of company***

Section 13(2) of the Companies Act, 2013 provides that the company can change its name only after complying with the provisions of Section 4 and after getting the approval of the Central Government in writing. However, if the change in name of the company merely involves the addition or deletion of the word 'Private' resulting from the conversion of a company from public to private or private to public, then the approval of the Central Government may not be taken.

Section 4(2) provides that the name of a company shall not be identical with or too closely resemble the name of an existing company. Moreover, the name shall not be such that its use by the company would amount to an offence under the law in force in India. The name shall not be undesirable in the opinion of the Central Government.

Section 4(3) provides that no company shall adopt a name that indicates that the company has any connection with the Central Government or any of the state governments or local bodies.

The Registrar of Companies enters the new name of the company in the register of companies and issues a fresh certificate of incorporation reflecting the new name of

the company.

Effect of change in name clause

It is pertinent to note that a change in the name of the company does not affect the rights or obligations of the company. All legal proceedings initiated against the company by its former name would continue against the company by its new name. Even after the change in name of the company, if any person initiates a suit against the company by its former name, it would be considered a curable defect and would not amount to the initiation of a suit against a non-existent person. However, a company cannot initiate a suit under its former name after adopting a new identity.

- ***Change in registered office***

  Change from one state to another

  A company can shift its registered office from one state to another only after passing a special resolution to that effect and after obtaining the prior approval of the Central Government. Once a company files an application for a change of registered office with the Central Government, the Central Government shall dispose of the application within a period of 60 days.

  The Central Government, before granting its approval, would make sure that the company had the approval of its creditors and debenture holders for the change of registered office. A change in the registered office of the company does not merely affect the shareholders of the company; it also impacts the creditors and employees of the company. Thus, in many cases, resolutions permitting the transfer of registered offices are challenged by employees, creditors and minority shareholders. However, the courts are usually reluctant to interfere with the wisdom of the company reflected in the special resolution.

  Section 13(4) states that if the company is shifting its registered office from one state to another, then the approval of the Central Government will have to be filed with the Registrars of both states. The new certificate of incorporation will be issued by the Registrar of the state to which the office is being shifted.

  Change within the same city or town

  It is pertinent to note that the company can shift its registered office from one place to another within the local limits of the same town, city or village without passing a special resolution. In this case, the company will have to hold a Board meeting and pass a Board Resolution authorising the change in registered office. Thereafter, the company will have to file Form INC-22 with the Registrar. The company has to inform the Registrar of the new address within 15 days of the change in registered office.

Change from one city to another within the same state

If a company is shifting its registered office from one city to another in the same state, then it will have to pass a special resolution amending its MoA. However, the approval of the Central Government is not required in this case.

It is pertinent to note that the MoA has to be altered only if the registered office is being shifted from one state to another. A change of registered office within the same state does not require an alteration of the MoA. This is because the MoA only contains the name of the state in which the registered office is located and not the name of the city or town.

- ***Change in object clause***

If a company needs to venture into new areas of business, then it will also have to amend the object clause of the Memorandum of Association. However, it is pertinent to note that if a public company has raised money through the issue of prospectus and has some unutilized funds, then, in order to amend the MoA, it will have to:

- Publish the details of the special resolution in 2 newspapers (one English and one vernacular language) that are in circulation in the area in which the registered office of the company is located. Moreover, the details will also have to be published on the website of the company.
- The shareholders who dissent from the special resolution shall be given an exit option.

Once the special resolution is filed with the Registrar, the Registrar has to certify the alteration of the MoA within a period of 30 days.

A company cannot adopt too broad object clauses. It has to specify the fields in which it undertakes to carry on business. In *Re Bhutoria Brothers* (1957), the Court held that a company cannot incorporate a single provision in its object clause stating – '*The Company will carry on all kinds of business*'. Such a provision would imply that the company could pursue any business conceivable under the sun. However, the Court also pointed out that a certain degree of flexibility can be allowed while drafting the object clause, and the company may provide that it would pursue any other business that may conveniently and advantageously combine with its existing businesses.

It is pertinent to note that one of the significant changes brought about by the 2013 Companies Act was that it simplified the process for the alteration of objects. The 2013 Act does not stipulate any requirement for sending information to individual creditors, bankers or other lenders. A mere publication of the proposed alteration in national newspapers would suffice.

2. ARTICLES OF ASSOCIATION

The Articles of Association of a company is one of the most essential documents of a company. It prescribes the rules, regulations and by-laws according to which the internal matters of the company are conducted. In simpler terms, it specifies the conduct of the business of a company and is a document of paramount significance for a company.

Under the Companies Act of 2013, Section 2(5) covers the definition of Articles of Association. According to the aforesaid Section, AOA or 'Articles' contain all the rules and regulations framed by the Directors of the company to govern the internal management and governance, which can also be altered from time to time.

An AOA is often compared to a rulebook of a company since it regulates the internal management of a company while also giving powers and obligations to its officers and employees. This includes regulations for several details of the company and its workings, such as rights of the shareholders, qualifications of directors, binding effect of contracts, etc. Moreover, the Articles of Association even establishes contracts between, firstly, members of the company, and secondly, members and the company.

However, it must be noted that while the AOA establishes the regulations of the company, it is still subordinate to the Memorandum of Association. MOA acts as a constitutional document of the company that supersedes all other documents within the company. If the AOA exceeds the scope laid down in the provisions of the MOA, then it would be considered *ultra vires,* as laid down by the Calcutta High Court in the landmark judgement of *Shyam Chand v. Calcutta Stock Exchange (1945)*. Thus, in the event of a conflict between the two, the provisions laid down in the Memorandum of Association would prevail. Further, in case of any uncertainty of such provision in the MOA, it shall be read along with the AOA for a more harmonious interpretation and understanding.

- ***Binding effect of Memorandum of Association (MOA) and Articles of Association (AOA)***

Once the Memorandum and the Articles of Association of a company are registered with the Registrar, both documents legally bind the company with its members. This binding effect is almost akin to a contract since it has much less force than a statute. This effect is explained in further detail as follows:

Binding the company to its members

The first binding effect both the MOA and the AOA have is between the company and its members. The members have the obligation to act and conduct their corporate affairs

within the scope of the MOA and the AOA. Meanwhile, the members can restrict the company from doing any actions in contravention of either the MOA or the AOA as an injunction. The members can also enforce their own rights mentioned within the Articles of Association, such as the right to their declared dividends and shares in the company.

However, only a member or a shareholder of the company can restrict the company by enforcing the clauses under the AOA. As seen in the case of *Wood v. Odessa Waterworks Co. (1889)*, The AOA of the Defendant company stated the Directors can declare the payment of the dividends to its members and shareholders, with the official approval of the company at a general meeting. However, a resolution was passed that permitted the payment of dividends through debenture bonds instead of cash. The Court held that the term 'payment' referred to the payment in cash and thus, such resolution was held void. In simple terms, the Directors were restricted from executing the resolution since it went against the provisions of the AOA.

Members bound to the company

As mentioned earlier, the first binding effect is always between the company and its members. It is like a contractual relationship with both parties having their rights and obligations mentioned in the provisions of the AOA. Each member or shareholder of the company shall abide by the provisions of the MOA and the AOA. This includes when any member has any amount payable to the company, which shall be considered a debt due.

In the case of *Borland's Trustee v. Steel Bros. & Co. Ltd. (1901)*, the AOA stated that in case any member of the company went bankrupt, their share would be sold at the price decided by the Directors of the company. Thus, when the member Borland declared bankruptcy, Borland's Trustee (the plaintiff, in this case) asked to sell Borland's shares at their original value. The trustee further contended that since he was not a member, he was not restricted by the AOA.

It was, however, held that while the trustee may not be bound by the AOA, the shares that were bought were bound by its provisions. In simpler terms, the sale of the shares was to follow as per the provisions given under the Articles.

Binding between members

The second binding effect that the Articles of Association have is on the members of the company with each other. Such powers or rights can only be applied by and against a member of the company. However, it is often noticed that the Courts tend to extend the scope of such binding effect even to the individual members who are not exactly members of the company.

As seen in *Rayfield v Hands (1960)*, the plaintiff was a shareholder of a company. The AOA of the company stated that if any shareholder wanted to transfer their shares, the Directors of the company would have to buy such shares at a reasonable and fair value. Following this provision, the plaintiff informed the Directors, who refused to pay for his

shares and argued that it was not within their obligations.

However, the judgement was given in favour of the plaintiff as the High Court stated that the plaintiff was not required to join the company as a member to bring a suit against it. The Directors were ordered to buy the shares of the plaintiff at a fair rate.

No binding in relation to outsiders

Any third party or individual not connected to the company shall not be bound by the AOA or the MOA of the company. Neither the company nor its members are bound to such third parties within the scope of the Memorandum and the Articles. As seen in the case of *Browne v. La Trinidad (1887)*, the AOA of the company contained a clause that implied the plaintiff may be a Director that should not be removable. However, he was still removed later and proceeded to sue the company for the contravention of the Articles.

It was held by the House of Lords that since the plaintiff was an outsider to the company, he could not restrict the company since he would not have any rights to enforce as a member. In simple terms, an outsider to the company cannot take undue advantage of the AOA to restrict or enforce any claims against the company.

- *Doctrine of constructive notice*

According to Section 399 of the Act, after the registration of the MOA and the AOA of any company with the Registrar, it becomes a public document that can be easily accessible by any member of the public at a prescribed fee for accession. Once such a request is made to any company, as per Section 17 read with Rule 34 of Company (Incorporation) Rules, 2014, the company has the obligation to send that individual a copy of its MOA, AOA and all the other agreements mentioned under Section 117(1) of the Act. However, if the prescribed fee is not paid with such a request, the company has no obligation to send anything.

Thus, since both the MOA and the AOA become public documents, they are easily accessible to all the members of the company as well as anyone outside the company. In such a case, the doctrine of Constructive notice states that the company shall deem the party dealing or contracting with the company to have read such public documents or, at least, be aware of its provisions. This knowledge is important since the AOA can directly affect the contractual obligation of the company.

The individuals or third parties dealing with the company can request to access the MOA and the AOA just as any other member of the public. If the company fails to provide copies of the aforesaid documents, then every defaulting 'officer' of the company who fails to do so may be liable to a fine of Rs. 1000 for each day of default until it is resolved. Or it can be extended to one lakh rupees, given whichever is less.

In the end, it is the duty of every person planning to interact or contract with the company to inspect these aforementioned documents which are easily accessible to

the general public. Their knowledge of the workings of the company and its objectives would be assumed since the conducting of such due diligence is their responsibility.

Whether the individual has actually read the document would not matter since it would be assumed still that they are familiar at least with the relevant provisions in the Memorandum and the Articles of Association of the company. In this context, the MOA and the AOA act as a 'constructive notice' to the public and interested parties for the workings of the company.

As seen in the case of *Kotla Venkataswamy v. Chinta Ramamurthy (1934)*, the Article of the Association of the company of the Defendant stated that if any property of the company is mortgaged, then such mortgage deed would require the signatures of the Company's Secretary, Managing Director and the Working Director. Without all three signatures, the deed would not be held valid.

In the present case, the plaintiff had filed the suit to enforce her tenancy rights but it was later found that the mortgage deed only had the signatures of the working Director and Company Secretary. Without the signature of the Managing Director, the deed was accepted by the plaintiff. The Madras High Court held the mortgage deed invalid, stating that the plaintiff should have practised due diligence and had knowledge of the provisions of the AOA of the company, which is publicly available.

- ***Doctrine of indoor management***

The Doctrine of Indoor Management was first laid down in the case of *Royal British Bank v. Turquand (1856),* due to which it is also commonly referred to as the 'Turquand Rule.'

In this case, the Articles of Association of the Appellant company permitted the Directors of the company to borrow bonds by passing a resolution in the general meeting. However, the Directors had given a bond without the passing of such a resolution, resulting in the present suit. The issue that arose was whether the company would be still liable for such a bond or would the transfer be invalid due to the conduct going against the AOA of the company. The (then) Chief Justice, Sir John Jervis held the company liable, stating that the individual receiving the bond was entitled to assume that the prescribed procedure in the AOA was followed and the bond was given in good faith.

This judgement was held quite ahead of its times and was not fully accepted or incorporated into the common law until the case of *Mahony v. East Holyford Mining Co. (1875)*.

The House of Lords, in the present case, endorsed the Turquand case and explored the concept of indoor management, which is quite opposite to the the doctrine of constructive notice. Simply put, while the Doctrine of Constructive Notice protects the

company from the actions of an outside party, the Doctrine of Indoor Management protects the third parties not connected to the company from the company. It is so since the Constructive Notice is solely restricted to matters outside of the company, which has an external position and does not regard the internal mechanism of the company.

Meanwhile, the Doctrine of Indoor Management protects the third party from any default in the inner workings or mechanisms of the company that any outsiders would not be aware of despite practising proper due diligence. If the contract between the company and any third party is consistent with the public documents of the company, then it shall not be prejudiced due to any irregularities arising on the part of the inner workings or 'indoor' operations of the company.

From the common law, this doctrine has also been adopted into Indian Law, as seen in the cases of *Official Liquidator, Manabe & Co. Pvt. Ltd. v. Commissioner of Police (1967)* and *M. Rajendra Naidu v. Sterling Holiday Resorts (India) Ltd. (2008)*, where it was held that while the individuals or third parties lending to the company should be familiar with the MOA and the AOA of the aforesaid company, they should not be expected to know every single inner working of the company. In simpler terms, third parties dealing with the Companies are not obligated to be acquainted either each and every internal action and proceedings occurring in the company.

Exceptions to the Doctrine of Indoor Management

a. *Where the outsider is aware of the irregularity*

While third parties are not expected to be aware of the internal workings or actions of a company, if the knowledge of such irregularity is with the party, then they shall not have the protection of the Doctrine of Indoor Management. In simpler terms, if the third party gets to know about the irregularity in the internal procedure, even in an implied manner through their observation of lack of proper process or authority followed, then it is their duty to not go through with the transaction. If the third party still decides to go with the transaction, they would not be protected under the scope of this doctrine.

As seen in the case of *Howard v. Patent Ivory Co. (1888)*, the AOA of the Defendant company allowed the Directors of the company to borrow up to one thousand pounds and not beyond that. To exceed that amount, they need to pass a resolution in the general meeting, which was not followed through by the Directors before they borrowed 3500 pounds in exchange for debentures from the plaintiff, who was one of the Directors present on the Board.

The present suit came to be when the company refused to pay back such an amount and the judgement was held in the favour of the company, stating that the debentures would only be paid up to the amount of 1000 pounds since the plaintiff had full knowledge of the irregularity of internal procedure as a Director.

b. *Lack of knowledge of the AOA*

As mentioned earlier, this Doctrine cannot protect anyone who has not acquainted themselves with the AOA and the MOA of the company despite both being available in public records. As seen in *Rama Corporation v. Proved Tin & General Investment Co. (1952)*, the plaintiff Corporation did not acquaint themselves with the Articles of Association of the Defendant company while doing a transaction with them.

c. Negligence

The Doctrine of Indoor Management does not protect third parties who have not practised proper due diligence. In simpler terms, if the irregularity could have been noticed with proper due diligence or observation on the side of the third parties, then this doctrine does not protect such parties as a consequence of their blatant negligence.

As seen in the case of *Al Underwood v. Bank of Liverpool (1924)*, the officer of the Defendant company had taken actions which were not within their scope of duties. However, the plaintiff did not ensure if the officer contracting with them as the representative of the company was duly authorised, resulting in negligence on their end due to which they were not protected under this doctrine.

d. Forgery

Any illegal transactions or transactions involving forgery are not protected under this doctrine. In simpler terms, if there is any forgery that results in a fraudulent transaction where the company had no idea or will would not be protected by the Doctrine of Indoor Management.

As seen in the *Ruben v. Great Fingall Consolidated (1906)* case, the secretary of the Defendant company had forged the signatures of the Directors on a certificate to issue shares of the company. It was held that since the Directors had no hand or idea of such forgery, they could not be held liable for the fraudulent transaction happening due to it. Furthermore, the forged share certificate was held to be void and hence, would not invoke the Doctrine of Indoor Management. The unauthorised use of the company seal can also be included within the scope of this exception along with the cases of Oppression.

This exception of the doctrine also includes situations where a third agency was involved in the transaction, as seen in *Varkey Souriar v. Keraleeya Banking Co. Ltd. (1956)* case, where agents of the company had acted on their own without the authorisation of the Defendant company.

3. PROSPECTUS

A prospectus is a document issued by a company to invite deposits or subscriptions from the public by way of issuing securities of the company. It can be understood as a

document or a booklet containing crucial information about the company and its securities for potential investors. Section 2(70) of the Companies Act, 2013 defines a prospectus as *"prospectus means any document described or issued as a prospectus and includes a red herring prospectus referred to in section 32 or shelf prospectus referred to in section 31 or any notice, circular, advertisement or other document inviting offers from the public for the subscription or purchase of any securities of body corporate"*

- ***Meaning and purpose of a prospectus under Company Law***

From the perspective of the issuer

A prospectus is a document that provides all the essential information about the company at the time of raising an investment from the public. It can be understood as an invitation to offer the securities of the company. The public intending to invest in the company can make an offer above the offered price but within the price band. It is upon the company to allot shares to the public in the manner it deems fit. Every time a company has to raise an investment from the public, it is the duty of the company to inform the public about its financial position and the purpose of the investment. A prospectus is the first document through which a company publicises or discloses its financial and other relevant information.

Section 28(2) of the Companies Act, 2013 provides that any document through which an offer for sale is made to the public shall be deemed a prospectus. It is pertinent to note that the document has to be issued to the public and not a particular set of persons. Even if an advertisement is made in a newspaper regarding certain shares left for purchase by the company, it shall constitute a prospectus, as has been held by the Hon'ble Calcutta High Court in *Pramatha Nath Sanyal v. Kali Kumar Dutt (1924)*. From the perspective of the Investor

In order to be able to make an informed decision regarding an investment, an investor must have access to all the information about a company before investing in it. Institutional investors might receive such information without much trouble. However, it is the retail investors whose interest might be compromised if such information is not provided in due course. Thus, a prospectus becomes the most crucial document for any investor intending to invest in a company. This is also the reason why the company law mandates the filing of a prospectus every time before raising a public investment. It can also be safe to infer here that issuing a prospectus is one of the means of ensuring good corporate governance practices in a company as it encourages transparency, accountability and responsibility.

- ***Golden Rule by VC Kinderseley***

The 'Golden Rule' of the prospectus was propounded by Judge VC Kinderseley in the landmark judgement of *The New Brunswick Railway Company v. Muggeridge (1859)*. In this case, it was held that *"Prospectus is one of the means by which the investor is informed about the soundness of the company's venture."* The essence of the rule is that it is mandatory on part of the company to issue a prospectus; it is not only required to accurately put forth all the relevant facts and information but also ensure that it does not hide any information which might affect the decision of an investor. The rule is also known as the 'Golden Legacy' as has been described by Judge Pagewood in *Henderson v. Lacon (1865)*.

This aforementioned rule has been reflected under various provisions of the Companies Act, 2013 which seeks to protect the interests of investors by providing comprehensive and elaborative guidelines and requiring relevant disclosure of material facts to ascertain the financial soundness of a company.

- ***Contents***

For filing and issuing the prospectus of a public company, it must be signed and dated and contain all the necessary information as stated under Section 26 of the Companies Act, 2013:

1. Name and other crucial information, such as the registered address of the office, its secretary, auditor, etc.;
2. The dates of issue, including the opening date and the closing date;
3. Undertakings of the Board of Directors regarding separate bank accounts for the purpose of keeping receipts of the issue;
4. Undertakings of the Board of Directors regarding the details of utilisation and non-utilisation of receipts of previous issues;
5. Consent of the directors, auditors, and bankers to the issue, and expert opinions;
6. The details of the resolution passed for the issue;
7. Procedure and time scheduled for the allotment of securities;
8. The capital structure of the company;
9. The objective of the issue;
10. The objective of the business and its location;
11. Particulars related to risk factors of the specific project, gestation period of the project, any pending legal action and other important details related to the project;
12. The amount is payable on the premium;

13. Details of directors, their remuneration and the extent of their interest in the company;
14. Reports for financial information such as auditor's report, report of profit and loss of the five financial years, business and transaction reports, statement of compliance with the provisions of the Act and any other report.

As per Section 26(4) of the Companies Act, 2013, the company issuing the prospectus has to deliver a copy of the prospectus, signed by every person whose name has been mentioned in the prospectus as a director of the company or the attorney of the director, to the Registrar on or before the date of publication.

- ***Types of prospectus under Company Law***

The definition of prospectus under Section 2(70) is an inclusive definition. It provides that a prospectus shall include a Shelf Prospectus (as mentioned under Section 31), a Red Herring Prospectus (as mentioned under Section 32), or any other document inviting applications for subscription/purchase of securities of the company. The various categories of prospectus under the Companies Act, 2013 have been discussed hereafter.

a. Shelf prospectus

Drafting a prospectus is a cumbersome process as it requires a number of disclosures and information to be passed on to the investor. It may also be possible that a company makes multiple public offers in one financial year itself. In such a case, it will become nearly impossible for the company to draft an entirely new prospectus every time. Yet, it is also crucial to note that significant changes may take place in the financial status of the company. To balance the interests of the company as well as that of investors, the law provides for the concept of shelf prospectus.

Explanation to Section 31 of the Companies Act, 2013 provides that "*the expression "shelf prospectus" means a prospectus in respect of which the securities or class of securities included therein are issued for subscription in one or more issues over a certain period without the issue of a further prospectus.*" A company issues a shelf prospectus when it has to offer for subscription by the public, more than one round of issue. Shelf prospectus is a single prospectus that can hold good for multiple public offers.

The Securities Exchange Board of India (SEBI) shall have the power to prescribe the class or classes of listed companies that may be allowed to file a shelf prospectus. The validity of a shelf prospectus shall not exceed one year from the date of the first offer. The provision also provides a more stringent rule for disclosures by the company issuing a shelf prospectus.

An information memorandum has to be filed by the company while filing a shelf

prospectus, containing the following material facts:

- new charges created;
- all the changes in the financial position that have occurred after the first offer of securities or the previous offer of securities and before the succeeding offer of securities; and
- such other changes as may be prescribed.

Such an information memorandum must be filed with the Registrar within the prescribed time period (three months) prior to the issue of the second or subsequent offer made under the shelf prospectus.

Further, it is also the obligation of the company to inform an investor about the changes if they have been allotted the securities in advance before the adjustments. Further, based on such information, an investor has also given the right to withdraw their application and they will be refunded their money within fifteen days thereof.

b. Red Herring prospectus

Though most of us imagine big companies when talking about investments and funding, mid-size and small companies also require investments and they also make public offers. To safeguard their rights and enable them to have better access to finance, the law provides for red herring prospectus. Explanation to Section 32 of the Companies Act, 2013 provides the definition of a red herring prospectus as "*the expression "red herring prospectus" means a prospectus which does not include complete particulars of the quantum or price of the securities included therein.*" A red herring prospectus is a prospectus wherein information regarding either the quantity of securities or the price of securities is not disclosed by the company. Rather, the company only provides a price band. This enables a company to gauge the worth of its securities and enables them to achieve the requisite minimum subscription, which may not otherwise be possible had they already supplied the entire information .

A red herring prospectus is subjected to same regulations as a prospectus. It has to be filed before the Registrar of Companies at least three days before the issue has to be made public. Further, the company must file the complete details of the issue with the Registrar and the SEBI after the securities has been duly subscribed to.

c. Abridged prospectus

A prospectus could run into hundreds of pages in a single issue, which may prove to be a hectic task for retail investors. Retail investors, having limited access to financial knowledge as well as resources, might not be competent enough to understand the intricate details mentioned in the prospectus. A solution to this problem is an abridged prospectus.

Section 2(1) of the Companies Act, 2013 defines an abridged prospectus as a memorandum containing the salient features of an issue. The features to be included in an abridged prospectus are to be provided by SEBI. Further, Section 33 of the Act mandates for annexing an abridged prospectus along with form for application of purchase of securities. However, the proviso to sub-section (1) provides that this requirement may be dispensed with where the form of application was issued for:

- *"in connection with a bona fide invitation to a person to enter into an underwriting agreement with respect to such securities; or*
- *in relation to securities which were not offered to the public."*

Section 33(3) of the Act provides that if the company fails to comply with the provisions of abridged prospectus as discussed above, it shall be subjected to a penalty of up to Rs.50,000 for every default.

Deemed Prospectus

When a company wishes to issue its securities through an intermediary, the document containing the details of such securities is considered a deemed prospectus. Section 25(1) of the Companies Act, 2013 governs the deemed prospectus. The document shall be a deemed prospectus for the company whose securities are being offered to the public.

➢ ***Liability for misstatements in a prospectus under Company Law***

A prospectus is used by potential investors to gather information about the company. Thus, it is the duty of the company and its authorised persons to make true and correct statements in the prospectus. Generally, when false or incorrect information is added to the prospectus, it becomes a misstatement. Even an omission of important information amounts to a misstatement in a prospectus. Making a false or misleading statement thus entails certain liabilities. Under the Companies Act, 2013, there are two types of liability for misstatements in the prospectus.

a. Civil Liability

Civil liability under the Companies Act, 2013 is provided under Section 35. It provides that where a person has subscribed to the securities of the company acting on any misstatement included in the prospectus and has consequently suffered any loss, the company and the persons authorising the issue of such prospectus are liable for such loss, provided that certain conditions are fulfilled. These conditions include:

1. Subscription to the securities acting upon the misstatement

2. Loss or damages due to such misstatement
3. Knowledge of the Defendant must be proved by the Plaintiff
4. Such misstatement must be material to the facts

If the above conditions are met, the Plaintiff can claim remedies against the company as well as against the authorised personnel. The remedies include rescission of the contract, damages, and damages for the non-disclosure of material facts.

b. Criminal Liability

Apart from the civil liability in case of misstatements, Section 34 of the Act also provides the liability of the authorised personnel for the misstatements in the prospectus. Criminal liability has been provided under Section 447 of the Act. In case of fraud on the Plaintiff (investor of the company), a criminal suit can be filed against the following persons:

1. All the directors authorising the issue of the prospectus
2. All the proposed directors of the company
3. Each promoter
4. Any expert involved in the issue

Section 447 of the Act prescribes a minimum imprisonment of six months but not more than ten years, along with a fine which shall not be less than the amount of damages suffered but not more than three times of such amount. The proviso to the provision provides that in case the issue involves a public interest, the minimum term of imprisonment of the aforesaid persons shall be three years.

➤ Statement in Lieu of Prospectus

When a public company is formed and chooses not to issue a prospectus, it is legally required to submit a statement in lieu of a prospectus, which is also referred to as a substitute prospectus or substitute circular. This statement contains essential information about the company and its offering and must be filed with the registrar of companies to ensure transparency and compliance with regulatory requirements.

It serves as an alternative to a traditional prospectus, providing investors with necessary details while accommodating situations where a full prospectus may not be suitable.

Statement in lieu of prospectus means a statement instead of a prospectus. A statement in lieu of a prospectus is a statement issued by a public unlisted company

instead of a prospectus. It's a document prepared by public companies that don't issue a prospectus when they are formed.

This statement has all the information that a prospectus has and it is signed by all the directors of the public company or the directors-to-be. If the company doesn't file a statement in lieu of prospectus, it won't be allowed to allocate any shares or debentures.

Contents of Statement in Lieu of Prospectus

Information in the statement instead of a prospectus includes:

- Company Name.
- The company's share capital is divided into ordinary shares and the value of one share.
- Description of the planned activities and prospectus.
- Names, addresses, roles and responsibilities of proposed or appointed directors, officers, appointed lawyers and company secretaries.
- Rules for selecting and compensating these corporate representatives.
- Voting rights during company meetings.
- Quantity and value of shares and debentures intended to be issued.
- Names, jobs and addresses of those selling goods bought or offered for sale by the company.
- Amount to be paid in cash, stocks or bonds to each real estate seller.

Provision for Statement In Lieu Of Prospectus [Section 70, Companies Act, 2013]

Section 70 of the Companies Act, 2013 deals with statement in lieu of prospectus as:

A company with share capital that either doesn't issue a prospectus or has issued one but hasn't allocated any shares to the public must follow certain rules before allotting shares or debentures. At least three days before making the allotment, the company must submit a 'statement in lieu of prospectus' to the Registrar for registration.

This statement should be signed by every person listed as a director or proposed director of the company or by their authorised agent in writing. It should contain the details outlined in Part I of Schedule III and include the reports specified in Part II of Schedule III, while taking into account the provisions in Part III of that Schedule (Section 70).

When a private company transforms into a public company, it must provide the Registrar with a statement in lieu of prospectus. This statement should include the

particulars described in Part I of Schedule IV, along with the report outlined in Part II of Schedule IV, subject to the provisions in Part III of that Schedule (Section 44(2)(b)).

Failure to comply with these rules can result in a fine of up to Rs. 1,000 for the company and every director responsible.

If the 'statement in lieu of prospectus' contains false information, the person who authorised its submission can face imprisonment of up to two years or a fine of up to Rs. 5,000 or both. However, they can avoid liability if they can prove that the statement was not significant or that they had reasonable grounds to believe it was true. The legal and criminal consequences for incorrect statements or misrepresentations are the same as those for a prospectus (Section 70(5)).

Differences Between Prospectus and Statement in Lieu of Prospectus

The differences between prospectus and statement in lieu of prospectus are:

Purpose

A prospectus is a detailed document that provides information about a company's securities offering, while a statement in lieu of prospectus serves a similar purpose but is used in specific situations where a regular prospectus cannot be used.

Issuer

A prospectus is usually issued by a company that is going public or issuing new securities, whereas a statement in lieu of prospectus is issued by a company that is already publicly traded.

Content

A prospectus typically contains extensive information about the company's management, financial statements and the terms of the securities offering. In contrast, a statement in lieu of prospectus may have less detailed information.

Regulation

Prospectuses are subject to strict regulatory requirements and must be filed with the appropriate securities commission. Statements in lieu of prospectus may have fewer regulatory requirements.

Approval

A prospectus needs approval from the securities commission before it can be used, while a statement in lieu of prospectus may not require approval.

Distribution

A prospectus is usually distributed to potential investors, whereas a statement in lieu of

prospectus may not be widely distributed.

Timeframe

A prospectus is typically prepared and distributed when a securities offering takes place, whereas a statement in lieu of prospectus may be prepared and distributed at any time.

Purpose of use

Prospectuses are used to attract investment in securities, whereas a statement in lieu of prospectus is typically used for less formal purposes, such as enabling a company to make a public offering without the cost and time associated with preparing a prospectus.